No. 85-1153

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

PAPAGO TRIBAL UTILITY AUTHORITY,

Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT WITH A SUGGESTION OF SUMMARY DISPOSITION

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January 8, 1986

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

QUESTIONS PRESENTED

1. Whether the Court below exceeded its judicial function and usurped an administrative function by affirming a decision of the Federal Energy Regulatory Commission (Commission) on grounds which were expressly rejected by the agency?

2. Whether the Court below erred in holding that a lawful action of a utility is *per se* prudent even if it admittedly imposes unnecessary additional costs on ratepayers?

PARTIES BELOW

Arizona Electric Power Cooperative, Inc.
Arizona Power Authority
Arizona Public Service Company
Buckeye Water Conservation and Drainage District
Citizens Utilities Company
City of Wickenburg, Arizona
Colorado River Indian Irrigation Project
Electrical District No. 1
Electrical District No. 3
Electrical District No. 6
Electrical District No. 7
Federal Energy Regulatory Commission
Maricopa County Municipal Water Conservation District No. 1
Navopache Electric Cooperative, Inc.
Papago Tribal Utility Authority
Plains Electric Generation and Transmission Cooperative, Inc.
Roosevelt Irrigation District
San Carlos Indian Irrigation Project
Welton Mohawk Irrigation and Drainage District

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FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT WITH A SUGGESTION OF SUMMARY DISPOSITION

Papago Tribal Utility Authority (PTUA), the petitioner below, petitions for a Writ of Certiorari, With a Suggestion of Summary Disposition, to review the October 10, 1985 decision of the United States Court of Appeals for the Ninth Circuit in *Papago Tribal Utility Authority v. Federal Energy Regulatory Commission,* Case No. 84-7012. The Court's order affirms Opinions No. 193 and 193-A issued by the Federal Energy Regulatory Commission (the Commission) on October 19, 1983 and December 19, 1983, respectively, in which with respect to the issues raised by

PTUA, the Commission affirmed without discussion the February 25, 1983 Initial Decision of its Administrative Law Judge (ALJ). In this case, a public utility sold tax benefits for $50.625 million which admittedly caused its ratepayers a present value loss (in the form of higher tax allowances and rates) of $82.6 million. The ALJ ordered the sales proceeds amortized over thirty years with the deduction of the unamortized portion thereof from the utility's rate base. The ALJ and the Commission denied PTUA's request for full compensation to ratepayers for their actual loss on the ground that any lawful action of a utility was *per se* prudent.

OPINIONS AND ORDERS BELOW

The opinion of the United States Court of Appeals for the Ninth Circuit is reported at 773 F.2d 1056, and is reprinted in Appendix A.[1] The Commission's Opinions Nos. 193-A and 193 are reported at 25 FERC ¶61,393 and 25 FERC ¶61,092, respectively, and are set out in Appendix B and C. The ALJ's Initial Decision is reported at 22 FERC ¶63,062 and is set out in Appendix D.

JURISDICTION

The judgment of the United States Court of Appeals for the Ninth Circuit was entered on October 10, 1985. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1) and 16 U.S.C. §825*l*(b).

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[1]References to the Appendix to this petition are hereafter given as "(App. ___)".

STATUTES INVOLVED

The statutes upon which the Court of Appeals' decision is based are the Federal Power Act of 1935, 16 U.S.C. §824 *et seq.*, and the Economic Recovery Tax Act of 1981 (ERTA), 95 Stat. 172, P.L. 97-34. The relevant portions of both statutes appear in Appendix E.

STATEMENT OF THE CASE

Arizona Public Service Company (APS) sells electricity at retail and wholesale in the State of Arizona. Its wholesale sales are regulated by the Commission under the Federal Power Act. PTUA is an unincorporated agency of the Papago Indian Tribe organized to provide electrical service to the Papago Reservation, which is located near Tucson, Arizona. PTUA buys all of its electricity from APS.

On December 18, 1980, APS filed a rate increase of $14,736,554 with the Commission in Docket No. ER81-179 under Sections 205 and 206 of the Federal Power Act, 16 U.S.C. §§824d and 824e, respectively. (Certified Administrative Record, p. 5397)[2] The Commission set the matter for hearing, and a hearing was held before an ALJ in November and December of 1981.

On November 12, 1981, during the course of the hearing, APS sold investment tax credits (ITC) and Accelerated Cost Recovery System (ACRS) tax benefits related to its newly completed Cholla 4 steam

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[2]References to the Certified Administrative Record shall hereafter be designated (R. ___).

electric generating stations to General Electric Credit Corporation for $50,625,000 under the safe harbor lease provisions of the Economic Recovery Tax Act of 1981. (App. 41a). At the request of the Commission Staff, the ALJ severed the issue of the proper treatment in rates of the proceeds of this sale from the other issues in this docket and the rate proceeding was phased. All issues related to the safe harbor lease were to be considered in Phase II.

Hearings were held in Phase II during May, 1982. On February 25, 1983, the ALJ issued his Initial Decision in Phase II, 22 FERC ¶63,062 (App. 39a-67a). In the Initial Decision, the ALJ found that as a result of the sale of the tax benefits the tax allowances in APS' rates would be vastly increased over the life of the plant. (App. 54a) He found that the present value to ratepayers of the benefits sold was $123.5 million. (App. 54a) The Commission—which did not itself calculate the loss to ratepayers—found that even APS itself had concluded "... that the net present value of costs the ratepayers will incur is $82.6 million." (Footnote omitted) (App. 30a) This amount thus exceeds, by at least $30 million, the $50.625 million received by APS from General Electric. As a result, the ALJ found that APS' ratepayers would be forced to pay, over the life of the plant, millions of dollars in additional tax allowances which they would not have been required to pay had the transaction not occurred. (App. 54a-55a)

The ALJ ruled that APS must both amortize the proceeds every year against rates and reduce rate base by the unamortized balance of the proceeds. He refused, however, to require APS to reduce its rates sufficiently to make whole the ratepayers' loss. (App.

63a) He held that even though ratepayers had sustained a substantial loss by this transaction, APS had not been imprudent because the utility had no duty to avoid unnecessary tax costs when to pay them benefitted stockholders. (App. 56a)

PTUA filed exceptions to the Initial Decision. In its exceptions PTUA argued that APS had been imprudent in entering into a transaction which had such a negative effect on its ratepayers and that the Commission should require APS to shield its customers from the adverse effects of this transaction. Specifically, PTUA asked that APS' rates be reduced by a deduction of $137.8 million from rate base and that this sum be amortized by equal rate reductions over the thirty year tax life of Cholla 4. (R. 7304-5) Alternatively, PTUA requested that APS be permitted to retain the sale proceeds but that its rates be fixed as if the tax benefit sale had never occurred. (R. 7306)

On October 19, 1983, the Commission issued Opinion 193, 25 FERC ¶61,092, in which it affirmed the Initial Decision (App. 26a-38a). The Commission did not discuss the scope of relief issue in Opinion 193. PTUA filed a timely application for rehearing in which it reiterated these arguments. On December 19, 1983 the Commission issued Opinion 193-A, 25 FERC ¶61,393 (App. 19a-25a) in which it denied rehearing again without discussing the scope of relief issue. PTUA filed a timely petition for review with the U.S. Court of Appeals for the Ninth Circuit on February 17, 1984.

In the Court of Appeals, PTUA once again argued that APS had been imprudent in engaging in a transaction which imposed unnecessary additional costs on its ratepayers. (PTUA Brief, pp. 21-32) The Court of

Appeals issued its opinion on October 10, 1985. In that opinion, the Court held that PTUA could not overcome the ALJ's finding that because Congress intended in enacting ERTA to permit such transactions and allow the corporate taxpayer to retain the sales proceeds the transaction was not imprudent. Thus, the Court stated in its only discussion of PTUA's arguments on this issue:

> Papago also challenges the Commission's ratemaking treatment of the proceeds of the Cholla 4 transaction. It argues in reliance upon *Midwestern Gas Transmission Co. v. FPC*, 388 F.2d 444 (7th Cir.), *cert. denied*, 392 U.S. 928, 88 S.Ct. 2286, 20 L.Ed.2d 1386 (1968), that the Commission erred in limiting the rate adjustment to the dollar value of the sales proceeds rather than the full value of the tax benefits to the ratepayers. In *Midwestern*, the utility had reverted from liberalized depreciation to straight-line when the FPC required it to flow-through the tax savings resulting from use of the former method to its ratepayers. The court found that management had chosen "the one method certain to result in maximum tax costs to themselves, with resulting maximum rates to the consumers," *id.* at 448, and that the resulting increased tax cost was not a "reasonable and prudent business expense" which the ratepayers could be required to bear. *Id.*
>
> Papago contends that APS' sale of the tax benefits was imprudent under *Midwestern* because there was no legitimate business purpose for the sale. Papago claims that the sale

would have been proper only if APS could not have used the ACRS deductions and ITCs to reduce its taxes in the future. Papago is unable to overcome the ALJ's finding that the transaction was not imprudent because one of Congress' major purposes in enacting the safe-harbor leasing provision was to make it perfectly legal for corporations, including APS, to transfer future potential benefits into current income. *See* "General Explanation of the Economic Recovery Tax Act of 1981," Staff of the Joint Committee on Taxation, at 103 (December 29, 1981), *reprinted in* Internal Revenue Acts, 1980-81, at 1478. We therefore decline to disturb the ALJ's exercise of his sound discretion in concluding that APS acted prudently in selling its tax benefits to General Electric. (App. 17a)

REASONS FOR GRANTING THE WRIT[3]

1. The Court below, in affirming the Commission on grounds not advanced by the agency, usurped the agency's *administrative* powers[4] and exceeded the

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[3]As the ALJ noted the Safe Harbor Lease provisions of ERTA were repealed in 1982, the year after their enactment, in the Tax Equity and Fiscal Responsibility Act of 1982, P.L. 97-248, §209; 96 Stat. 324, 442 (1982). For this reason the specific fact situation involved herein is unlikely to recur, and we are aware of only one other case before the Commission in which this issue has arisen. *Cleveland Electric Illuminating Co.*, 28 FERC ¶63,089 (1984), *affd.*, 32 FERC ¶61,381 (1985). However, the principles involved in this Case are of enduring importance in the regulation of public utilities.

[4]*Federal Radio Comm. v. Nelson Bros.*, 289 U.S. 266, 274-276 (1933).

scope of its own limited statutory *judicial* powers under Section 313(b) of the Federal Power Act, 16 U.S.C. §825*l*(b), "to affirm, modify, or set aside" orders of the Commission.

The Court below affirmed the Commission because

> Papago is unable to overcome the ALJ's finding that the transaction was not imprudent because one of Congress' major purposes in enacting the safe-harbor leasing provision was to make it perfectly legal for corporations, including APS, to transfer future potential benefits into current income . . . We therefore decline to disturb the ALJ's exercise of his sound discretion in concluding that APS acted prudently in selling its tax benefits to General Electric. (Citations omitted) (App. 17a)

This holding is not an affirmance of the agency's findings because the only basis advanced by the ALJ as support for his conclusion that APS had not acted imprudently was that APS had acted in the best interests of its stockholders even though its action was contrary to the best interests of ratepayers.[5] There is no mention in the ALJ's decision—or anywhere else for that matter—that Congress intended corporate taxpayers to retain the financial advantages of sold

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[5]The ALJ held that

> A regulated public utility does not act imprudently merely because it fails to act in the best interests of its ratepayers in circumstances where those interests conflict with the corporate interests of the utility and its stockholders. (App. 56a).

tax benefits. In fact, both the ALJ and the Commission *expressly rejected* this thesis. The ALJ held:

> Finally, APS urges that deduction of the unamortized balance of the proceeds from rate base would eliminate any incentive on the part of public utilities to enter into safe harbor transactions, contrary to the intention of the Congress that enacted ERTA. Whether the Congress did intend to enact an affirmative spur to safe harbor transactions, rather than merely to allow them to take place is rather questionable. * * * * * It is significant, in this respect, that the Congress did not in ERTA mandate or prohibit any specific treatment of safe harbor proceeds in the hands of regulated public utilities. Since that same Congress included in the Act very specific directives with respect to the treatment of ACRS deductions and investment tax credits of regulated public utilities, it cannot be said that there was a lack of awareness on Congress' part of the risk that regulatory agencies might require substantial proportions of the benefits of the transactions to be flowed through to the ratepayers. This is, in short, a situation where congressional silence speaks volumes. The absence of a prohibition in ERTA on the reduction of rate base by the unamortized proceeds of safe harbor leases signifies that no such prohibition was intended. It also belies APS' argument that that treatment of the proceeds would seriously transgress the intention of the Congress that enacted ERTA. (App. 64a)

On APS' exceptions, the Commission held:

> As to the various arguments by all parties concerning Congressional intent in enacting ERTA, we agree with the judge's conclusion at page 17 of his decision that there is no real basis for interpreting a Congressional intent to preclude the rate treatment allowed herein. (App. 34a)

It is apparent from the ALJ's and the Commission's decisions that the Court below has affirmed the Commission's decision on grounds not only not relied on but specifically rejected by the agency.

In *SEC v. Chenery Corp.*, 318 U.S. 80, 88, 92 (1943), this Court held that an agency's decision may be affirmed by a reviewing court only on the basis of the grounds advanced by the agency. If the agency decision cannot be sustained on the basis of the reasons advanced therein, the reviewing court may not affirm the decision on the basis of other reasons supplied by it. Rather, it must remand the matter to the agency for another determination. Any other course would constitute an intrusion ". . . upon the domain which Congress has exclusively entrusted to an administrative agency." *Id.*, at 88. *See also, SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947); *Camp v. Pitts*, 411 U.S. 138 (1973). Consequently, the decision below must be summarily reversed on this basis.

2. If this Court believes that the decision of the Court below is properly rooted in the agency's rationale, the decision below must nevertheless be reversed because it is patently wrong as to the intent of Congress as the agency and the ALJ found.

In any event, the fact that APS' sale of tax benefits was lawful is irrelevant for all rate purposes. APS was under no legal compulsion to execute the GE safe-harbor lease, and it is clear beyond dispute that by making this tax benefit sale APS has imposed enormous unnecessary tax costs on its customers. The test of whether a utility has acted imprudently is not whether it has acted legally, but whether it has imposed unnecessary costs on the public. This Court so held in *NAACP v. FPC*, 425 U.S. 662 (1976). The NAACP had requested the Federal Power Commission to issue a generic rule making it an unlawful practice for utilities and pipelines under the Power Act and the Gas Act, respectively, to engage in racial discrimination. The FPC refused, holding that its authority over utilities' and pipelines' practices did not extend to employment practices. It also pointed to its practice of disallowing imprudently incurred costs including those related to racial discrimination. In affirming, this Court stated, at 666:

> The first of these statutory bases is the legislative command to the Commission under the Power and Gas Acts to establish "just and reasonable" rates for the transmission and sale of electric energy, 16 U.S.C. §824d(a), and for the transportation and sale of natural gas, 15 U.S.C. §717c(a), and, consequently, to allow only such rates as will prevent customers from being charged any *unnecessary or illegal* costs.[3] (Emphasis added)

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[3]See, *e.g.*, *Acker v. United States*, 298 U.S. 426, 430-431, 56 S.Ct. 824, 826-827, 80 L.Ed. 1257, 1261; *Cities Serv. Gas Co.*

This Court's holding was explicitly based on *Cities Service*, *infra*, which held that a lawful transaction could nevertheless be imprudent. Therefore, *NAACP* directly conflicts with the holding of the Court below that any lawful cost incurred by a utility is *per se* prudent and chargeable to ratepayers under the Federal Power Act. As this court expressly held the Power Act prohibits utilities from charging their customers with *either* "unnecessary or illegal" costs.

This principle was also applied in *Cities Service Gas Company v. FPC*, 424 F.2d 411, 417-418 (10th Cir. 1969), *cert. den.* 400 U.S. 801. There, a pipeline realized a substantial profit from the sale of certain gas producing properties but continued to buy the gas produced from such properties. The price paid for that gas after the sale of the properties was higher than the cost that would have been allowed had the pipeline continued its ownership and operation of the properties. The sale was admittedly legal, but the Commission refused to allow the higher costs to be passed through in rates. On review, the Court affirmed. It held, at 417:

> A regulated utility may not impose unnecessary costs upon its consumers . . . If the properties in question had been retained by Gas Company or an affiliate, cost of service would have determined the rate. We believe that the alienation of the properties to a non-affiliate, even though made in good faith and for value does not change the situation. The

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v. FPC, 424 F.2d 411 (CA10); *Safe Harbor Water Power Corp. v. FPC*, 179 F.2d 179 (CA3). See also n. 5, *infra*. (First emphasis added)

> parent company, Cities Service, received a $21,450,000 profit. Gas Company seeks a further profit by basing its gas cost on the price fixed by contract made between it and an affiliate and now binding on it and a non-affiliate. We believe that the use of the contract price can only result in a windfall to the Cities Service system through the imposition of increased charges on the consumers. (Citations omitted)

PTUA unsuccessfully urged the Commission (R. 7275) and the Court below (Br. 29-30) to adopt this sound and long recognized principle that unnecessarily incurred costs should not be allowed in rates. *Acker v. U.S.*, 298 U.S. 426, 431 (1936).[6] The rulings below directly conflict with holdings of this Court and of Courts of Appeals applying this principle to the tax allowance element of regulated utility rates. *El Paso Natural Gas Company v. FPC*, 281 F.2d 567, 572-573 (5th Cir. 1960) (all true tax savings belong to ratepayers); *Midwestern Gas Transmission Co. v. FPC*, 388 F.2d 444, 448 (7th Cir. 1968) *cert. den.* 392 U.S. 928 (higher taxes not justified by business purpose disallowed); *FPC v. United Gas Pipe Line Co.*, 386 U.S. 237, 244-245 (1967) (Commission power to limit cost of service to real expenses includes consolidated tax return savings).

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[6]We conceded that APS could have prudently participated in a safe-harbor lease transaction had it been able to demonstrate a good business purpose for it. Such a purpose might be an inability to use the ITC or ACRS benefits on its tax returns. However, it was proved at the hearing (R. 3026-3027) that such was not the case, and the ALJ rejected all other claims of good business purpose. (App. 54a-55a)

Therefore, the Court below erred in failing to require the Commission to provide ratepayers with a remedy for the unnecessary tax costs imposed on them, and this Court should reverse the Court below.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted. Since the Court below has exceeded its judicial function and usurped the Commission's administrative function and decided a federal question in conflict with applicable decisions of this Court and other Federal Courts of Appeals we suggest that this is an appropriate case for summary disposition by this Court. In the event the Court agrees with our suggestion, it may be appropriate to issue an order providing that the decision and judgment of the Court below be:

1. Summarily reversed because

   a. the Court of Appeals affirmed the agency on a ground it had not advanced, and had in fact specifically rejected, *SEC v. Chenery*, cited *supra*;

   b. the Court of Appeals erred in holding that a lawful action of a utility is *per se* prudent even if it admittedly imposes unnecessary additional costs on ratepayers. *NAACP v. FPC*, cited *supra*;

2. Remanded to the Court of Appeals for further action not inconsistent with the Court's order of summary disposition.

Respectfuily submitted,
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